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September 16, 2005

AGENDA ITEM 5.c.

TO: MEMBERS OF THE INVESTMENT POLICY SUBCOMMITTEE

- I. SUBJECT:** Revision of International Equity Real Estate Policy
- II. PROGRAM:** Real Estate (Core and Non-Core)
- III. RECOMMENDATION:** Approve the reading and recommend to the Investment Committee approval of the Statement of Investment Policy for International Equity Real Estate

IV. ANALYSIS:

Background

At the June 10, 2005 Policy Subcommittee meeting the Equity Real Estate Policy was revised to allow for international investing in the Core Real Estate portfolio. This revision expanded the previous international reach of the Core portfolio beyond Canada and Mexico to countries on the Permissible Equity Market List. The Policy Subcommittee approved the revision contingent upon updating the International Equity Real Estate Policy to allow for smooth cross referencing and clear governance between policies as well as to clarification of the means of managing the risks of international real estate investment.

Recommendation

Staff approached the task by generally cleaning up the discord between policies and by further clarifying the means of managing the risks of international real estate investment. Staff outlines these proposed changes here in the order that they appear in the policy.

First, Staff recommends the addition of further procedural clarification in the sections in the policy on benchmarking. Staff recommends that the NCREIF index remain applicable as a benchmark until more appropriate alternatives are identified. Staff is reviewing supplemental international benchmarks with PCA, namely the IPD or International Property Databank. Staff is currently discussing with IPD the customization of benchmarks to follow specific country groupings or

the use of amalgamated regional benchmarks. Staff is awaiting PCA's recommendation for the final determination on international benchmarking.

Second, Staff addresses currency issues by adding a section to the policy on currency management. In the interim, prior to implementation of the below, Staff and the Board's Consultant will coordinate appropriate strategies. In the longer term, the Real Estate Unit will periodically report all currency exposures to the Global Fixed Income, International & Currency Unit (GFI). GFI may analyze specific and aggregate currency exposures and recommend appropriate hedging strategies to the Chief Investment Officer (CIO) and Senior Investment Officer (SIO) of Real Estate. Upon CIO and SIO Real Estate approval, Real Estate Staff will coordinate with GFI to implement the approved strategies.

Third, Staff recommends removing the concept that international real estate investments shall be classified as Non-Core investments. International real estate investment now applies to both Core and Non-Core portfolios.

Finally, Staff recommends relocating the allocation range for the real estate portfolio from the International Equity Real Estate Policy to the Equity Real Estate Policy.

Attached is a blackline of the International Equity Real Estate Policy with the recommended language changes.

Also attached is PCA's concurrence letter with Staff's recommendations. Staff and PCA are available for any questions the Policy Subcommittee may have.

Please see also the related Equity Real Estate Agenda item number 5.b..

V. STRATEGIC PLAN:

This item supports Goal IV to assure that sufficient funds are available, first to pay benefits and, second to minimize and stabilize employer contributions.

VI. RESULTS/COSTS:

The actions described herein should streamline real estate policies, enhance risk mitigations for the portfolio capital allocations within the real estate portfolio, facilitate investment diversification, and enhance investment return.

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